(23) (19)



Nos. 91-1111 and 91-1128

In the

# Supreme Court of the United States

October Term, 1992

HARTFORD FIRE INSURANCE CO., et al.,

*Petitioners,*

v.

STATE OF CALIFORNIA, et al.,

*Respondents.*

MERRETT UNDERWRITING AGENCY MANAGEMENT LIMITED, et al.,

*Petitioners,*

v.

STATE OF CALIFORNIA, et al.,

*Respondents.*

**On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit**

## BRIEF FOR RESPONDENT STATES IN NO. 91-1111

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## QUESTIONS PRESENTED

1. Whether allegations that insurers' enlistment of reinsurers and others in agreements not to trade, as a means of compelling competitors to stop selling certain insurance products to American consumers, are sufficient to state a claim of "boycott, coercion or intimidation" within the meaning of section 3(b) of the McCarran-Ferguson Act.

2. Whether co-conspirators are liable for the antitrust injury that flows from conduct that is not regulated under section 2(b) of the McCarran-Ferguson Act.

3. Whether conduct regulated under section 2(b) of the McCarran-Ferguson Act loses its exemption when it is taken in furtherance of a conspiracy involving unregulated conduct.

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## STATEMENT

These cases concern the antitrust consequences that flow from the private regulation of American insurance markets by foreign and domestic insurers and reinsurers operating outside

state regulatory authority or control.[1] Reduced to essentials, the complaints allege that defendant primary insurers enlisted reinsurers "to compel capitulation" by competing primary insurers to the defendants' demands. *See* Hartford A-22a.[2] This private cartel intended to limit the scope of insurance products sold in the United States, *id.*, permitting the primary insurers to avoid competition from companies that would otherwise provide more desirable insurance products to consumers. Manifestly, these cases are not about the wisdom, utility or legality of standardized forms of insurance coverage, Hartford Br. 2-3; nor are they about isolated and unrelated occurrences in foreign insurance markets. Merrett Br. at 3 and Sturge Br. at 4-5.

### A. The Complaints.

The complaints allege that defendants Allstate Insurance Co., The Aetna Casualty and Surety Co., Hartford Fire Insurance Co. and CIGNA Corp. ("primary defendants") individually wanted to eliminate long-tail[3] and pollution insurance products from the commercial general liability ("CGL")

[1] These cases come before the Court on a record that has not been materially developed beyond the contours of the complaints. Defendants submitted the Affidavit of Carole Banfield ("Banfield Affidavit"), Joint Appendix at 113, in support of their McCarran-Ferguson Act motion. That affidavit was limited to uncontested details of the state regulatory systems, however. It did not address any of the market-related boycott activities that form the basis for the plaintiffs' claims for relief.

[2] This brief employs the following abbreviations: "JA" refers to the Joint Appendix; "Hartford A" refers to the Petition Appendix in No. 91-1111; "Hartford Br." refers to Brief for Petitioners in No. 91-1111; "Merrett Br." refers to Brief for Petitioners in No. 91-1128; and "Sturge Br." refers to Brief for Petitioner Sturge Reinsurance Syndicate Management Limited in No. 91-1128.

[3] Long-tail products cover risks for which claims may be filed many years after the occurrence giving rise to such claims. Conn. Compt. ¶ 4(v); Ca. Compt. ¶ 4(h).



insurance[4] market. Conn. Compt. ¶¶ 65 and 67; Ca. Compt. ¶¶ 61 and 63. Unilaterally discontinuing these products could have cost the four firms significant market share.[5] Thus, the primary defendants could not stop selling these products unless their competitors were also willing to forego these sales. *See, e.g.*, Conn. Compt. ¶¶ 68, 73 and 74; Ca. Compt. ¶¶ 64, 69 and 70.

Unable to obtain voluntary agreement from their competitors, the primary defendants began organizing the conspiracy to purge long-tail and pollution insurance products from the market. Conn. Compt. ¶¶ 66 *et seq.*; Ca. Compt. ¶¶ 63 *et seq.* To force all insurers to abandon these products, the primary defendants sought to control two critical inputs in the insurance industry: reinsurance and statistical support, both needed by competitors to underwrite policies profitably. Conn. Compt. ¶¶ 4(p), 48, 51-52, 103; Ca. Compt. ¶¶ 4(o), 39, 42-43, 99.

Reinsurance[6] is essential to insurance markets. *See* Conn. Compt. ¶¶ 4(p) and 73; Ca. Compt. ¶¶ 4(o) and 34. An insurer can greatly expand its capacity to insure various risks through the purchase of reinsurance. Conn. Compt. ¶ 4(p); Ca. Compt. ¶ 29. Lack of reinsurance would force even some of the largest companies to reduce sales drastically and chance the permanent loss of established clients. *Id.; see* 1 B. Webb, H.

[4] Commercial general liability insurance provides coverage against third-party claims for businesses and state and local governments. Conn. Compt. ¶ 4(a); Ca. Compt. ¶ 4(a).

[5] Defendants understood the nature of the marketing disadvantage they would face without competitor acquiescence. *See* David C. Sterling, Secretary at The Hartford Insurance Group, Monograph 9, "Environmental Impairment Liability: An Insurance Perspective," contained in *Issues in Insurance*, Vol. II, at 210 (E. Randall, ed., 4th ed., 1987) ("From a [seller's] standpoint, the selling of pollution liability insurance makes sense because the coverage can be used as a door opener for new business as well as for various target marketing opportunities.").

[6] Reinsurance is an agreement whereby one party (the reinsurer) agrees to reimburse another party (the insurer) for a designated portion of the risks underwritten by the insurer. Conn. Compt. ¶ 4(p).

Anderson, J. Cookman & P. Kensicki, *Principles of Reinsurance* 5 (1990).

Reinsurance transactions occur primarily in interstate and foreign commerce. As defendants acknowledge, "To meet the needs of domestic primary insurers, much reinsurance must be placed abroad." Hartford Br. 2. Reinsurance transactions are not, in any case, subject to state insurance regulation. Conn. Compt. ¶¶ 41(e) and 46; Ca. Compt. ¶¶ 37 and 49(e); *see* States' Reg. App. ¶ E, JA 226, 228, 234, 241, and 247.[7]

Statistical support services are also essential for marketing these insurance products. Conn. Compt. ¶ 103; Ca. Compt. ¶ 99. Using statistical data provided by a rating bureau, an underwriter can price a particular risk with a high

[7] Reinsurers have historically conducted their affairs subject to antitrust rules. N. David Thompson, president and chief executive officer of Defendant North American Reinsurance Corp., expressed this view in *Forum*, a publication of the American Bar Association:

> Reinsurers have generally conducted their operations free from the type of regulation to which primary insurers are subject in most jurisdictions. Reinsurance rates are not approved or filed. Reinsurance treaty provisions are not governed by statute or regulation, except for special matters such as the nearly universal solvency clause. . . . Thus, reinsurers have been outside the protections of the McCarran Act and so, at least, since the decision in the *South Eastern Underwriters* case, they are fully exposed to the enforcement of the antitrust laws, state as well as federal.

N. David Thompson, *Critical Issues of the Eighties: How Trends in Reinsurance Will Affect Legal, Legislative, and Regulatory Actions*, 16 Forum 1038, 1055 (1980-1981) (footnote omitted). *Accord*, C.F. Aldrich [president of Kemper Reinsurance Co.], "Regulation, Accounting, and Statistics," in R.W. Strain, *Reinsurance* 621 (1980) ("[R]einsurance has been traditionally subject to little, if any, specific state regulations of the type contemplated by the McCarran Act."); 1 J. Atwood and K. Brewster, *Antitrust and American Business Abroad* 78-79 (2d ed. 1981) ("[S]ince state insurance schemes do not, and could not, purport to regulate the bulk of international insurance transactions, the federal antitrust laws are fully applicable. This may be one area where the international nature of the transaction enhances antitrust risks.").



probability that, on average, premium income from that and similar risks will exceed claims. The underwriter's confidence in the price and the insurer's consequent willingness to write the policy depend upon the size of the statistical database available. This must be large enough to provide a credible appraisal of the risk in question.[8] *See id.*

Defendant Insurance Services Office, Inc. ("ISO") is the almost exclusive source of statistical support services in this country for CGL insurance. Conn. Compt. ¶ 4(e); Ca. Compt. ¶¶ 38-39. ISO has approximately 1,400 insurer members, including the four primary defendants. *Id.* By sharing the claims experience of its entire membership, ISO is able to provide a statistical database to its members that would be difficult for any single company to match. Conn. Compt. ¶ 103; Ca. Compt. ¶ 99. With the exception of the few very largest insurers, like the primary defendants, no individual insurer is capable of creating a database of its own that would be reliable for underwriting CGL policies. *See* Conn. Compt. ¶¶ 103-04; Ca. Compt. ¶¶ 99-100.

The complaints specifically allege that by December 1983, the four primary defendants had agreed to eliminate long-tail and pollution insurance entirely from the American market for CGL insurance. The then-voluntary ISO form revision process, begun in 1977, was close to completion and ISO was preparing to propose new CGL forms. Conn. Compt. ¶ 59; Ca. Compt. ¶ 55. Despite the primary defendants' objections, their competitors had approved new forms that retained long-tail and pollution coverage. Conn. Compt. ¶ 66; Ca. Compt. ¶ 62.[9] In March 1984, notwithstanding primary

[8] 2 B. Webb, J. Launie, W. Rokes & N. Gablini, *Insurance Company Operations*, 37-39 (1984). Contrary to defendants' unsupported factual statement that most long-tail risks are "unforeseeable . . . and hence not reflected in the underwriting decision or the premium charged," Hartford Br. 4, a fully developed factual record will show that the vast majority of long-tail risks are both foreseeable and reflected in underwriting decisions and the premiums charged.

[9] Defendants imply that the American CGL market can only support one standardized form. Hartford Br. 2-3. That inference is neither supported by the record, *see* Banfield Aff. ¶ 4, JA 114, nor consistent with

defendants' continued objections, ISO began filing with State regulators a revised occurrence form and a claims-made form, both of which included coverage for long-tail and pollution risks.[10] Conn. Compt. ¶¶ 60, 63-65; Ca. Compt. ¶¶ 56, 59-61. Although ISO believed substantial time would be needed for education of industry groups and for regulatory review of the new forms, in its cover letter to State regulators, it "propose[d] that the new forms become effective . . . . " Banfield Aff. Ex. D. at 42, Docket Entry 515.

Having failed to attain their goal through voluntary persuasion within ISO, the primary defendants turned to concerted, coercive enforcement efforts conducted outside the purview of state regulators to purge long-tail and pollution products from the American market. Beginning no later than March 1984, the primary defendants organized and entered into agreements with a reinsurance cartel to enforce their efforts to change the CGL market. Comprised of foreign and domestic reinsurers, the cartel was designed to change the CGL market by compelling the elimination of long-tail and

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ISO's promulgation of two CGL forms, Conn. Compt. ¶ 60; Ca. Compt. ¶ 56. The standard text for the Chartered Property Casualty Underwriter professional designation course of the American Institute for Property and Liability Underwriters, 1 B. Webb, J. Launie, W. Rokes & N. Baglini, *Insurance Company Operations* 8 (1984), recognizes that "[m]any insurers use both [standard and non-standard] types of forms" for different risks. Many non-standard forms "deviate only slightly from standard forms." *Id.* at 6. However, this case is not about the existence or voluntary use of standardized forms. This case is about denying competitors access to reinsurance and statistical support for the particular insurance products against which defendants Hartford, Aetna, Allstate and CIGNA did not want to compete.

[10] Occurrence based insurance covers liability arising from any event that transpired during the policy period regardless of when a claim for such liability is filed. Conn. Compt. ¶¶ 4(m) and 61. Claims-made insurance only covers claims filed during the policy period regardless of when the liability event occurred. Conn. Compt. ¶¶ 4(a) and 61-62.



pollution insurance products. Conn. Compt. ¶¶ 67-81; Ca. Compt. ¶¶ 63-77.

Defendants first directed their attention to ISO. Conn. Compt. ¶¶ 67-86; Ca. Compt. ¶¶ 63-82. ISO members were told that if they did not eliminate long-tail and pollution products from ISO's proposed new forms, there would be no reinsurance. *Id.* The cartel's coercive threats to withhold reinsurance from the American market escalated from March through September, 1984. By September 20, 1984, the reinsurance lock-out had its intended effect. ISO capitulated and actively joined the conspiracy. Conn. Compt. ¶¶ 88-89; Ca. Compt. ¶¶ 84-85. The conspirators' forms eliminated pollution insurance coverage; their claims-made form eliminated long-tail coverage.[11] Conn. Compt. ¶ 88; Ca. Compt. ¶ 84.

Eliminating long-tail and pollution coverages from ISO's forms did not guarantee that non-conspiring primary insurers would refrain from selling these products that consumers desired. Continued use of the 1973 ISO CGL form or the use of special endorsements could still have provided pollution or long-tail coverage. Moreover, an occurrence form of coverage remained available.[12]

Before 1986, most CGL insurance in the United States was sold on the 1973 ISO CGL form, which included coverage for both long-tail and pollution risks. Conn. Compt. ¶¶ 4(l), 47, 56 and 57; Ca. Compt. ¶¶ 4(1), 38, 52 and 53. ISO's coerced adoption of the new forms, and the subsequent approval of those new forms by

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[11] By incorporating into a claims-made policy a retroactive date, Conn. Compt. ¶ 4(q); Ca. Compt. ¶ 4(e), that is the same as the date of policy issuance or renewal, an insurer can limit coverage to circumstances in which both the liability event and claim filing must occur during the policy period. Conn. Compt. ¶ 63; Ca. Compt. ¶ 59. To eliminate long-tail risks from the market, defendants needed to promote the claims-made policy with retroactive date to the exclusion of all other products. Conn. Compt. ¶ 73; Ca. Compt. ¶ 69.

[12] While defendants succeeded in eliminating pollution from both the occurrence and claims-made forms and in inserting a retroactive date in the claims-made form, they did not succeed in forcing ISO to abandon the occurrence form entirely. Conn. Compt. ¶ 88; Ca. Compt. ¶ 84.

some of the states, did not remove the 1973 ISO CGL form from the market. Conn. Compt. ¶¶ 102-03; Ca. Compt. ¶¶ 98-99. Additionally, endorsements to the truncated ISO forms remained theoretically available for pollution and long-tail coverage. Banfield Aff. ¶ 15, JA 117-118. Defendants' further enforcement acts, however, guaranteed that neither the 1973 forms nor these endorsements could be used. Conn. Compt. ¶¶ 100 and 104; Ca. Compt. ¶¶ 96 and 100.

To ensure that competitors could not sell pollution or long-tail insurance products, primary defendants conspired with reinsurers to impose reinsurance cut-offs. Starting in 1984, contemporaneously with efforts directed at ISO, the reinsurer defendants, implementing their agreement with the primary defendants, began denying reinsurance to United States companies that chose to provide pollution insurance. Conn. Compt. ¶¶ 90-100; Ca. Compt. ¶¶ 86-96. By November 6, 1985, the otherwise competing foreign reinsurers agreed that all North American casualty reinsurance treaties, including coverage for CGL, would be written with a total pollution exclusion. Conn. Compt. ¶ 99; Ca. Compt. ¶ 95. As a consequence, pollution coverage evaporated from the CGL market. Conn. Compt. ¶ 100; Ca. Compt. ¶ 96.

In a related move, defendant reinsurers conspired with primary insurers to foreclose reinsurance support for companies providing long-tail insurance. Competitors of the primary defendants that continued to sell long-tail insurance would not receive reinsurance for it. Conn. Compt. ¶¶ 92-93; Ca. Compt. ¶¶ 88-89. Foreign reinsurers also imposed "sunset clauses" in reinsurance contracts. Conn. Compt. ¶¶ 94-96; Ca. Compt. ¶¶ 90-92. A "sunset clause" leaves an insurer "bare" if a long-tail risk develops after a designated period. No portion of the reinsurers' enforcement activity – whether threats or denials of reinsurance coverage, or their use of sunset clauses – was reviewed, approved, or otherwise regulated by any state. Conn. Compt. ¶ 46; Ca. Compt. ¶ 37.

As a result of defendants' manipulation of reinsurance, United States companies were effectively precluded from selling long-tail insurance and pollution insurance. That, in turn, foreclosed the possibility that the competitors of the



primary defendants could capitalize on the defendants' refusal to sell such insurance. *See* Conn. Compt. ¶¶ 4(p) and 100; Ca. Compt. ¶ 96; *see also supra* note 5. Even this success, however, did not end the defendants' enforcement acts.

The continued viability of the 1973 ISO CGL form prevented full realization of defendants' plan to force pollution and long-tail products from the market. Although lack of reinsurance would prevent competitors from selling these products in great quantities, competitors could still use the 1973 ISO CGL forms to sell them in limited amounts. Defendants, therefore, agreed to cut off statistical support for the 1973 form. Conn. Compt. ¶¶ 101-03; Ca. Compt. ¶¶ 97-99. Without statistical support, marketing coverages based on the 1973 form became, at best, imprudent. In short, the elimination of statistical support coerced insurers not to sell, and made consumers unable to purchase, long-tail and pollution insurance. *See* Conn. Compt. ¶¶ 103-04; Ca. Compt. ¶¶ 99-100.

After successfully forcing pollution products from the liability insurance market, defendants faced an additional problem. The unavailability of pollution coverage in liability policies might increase claims against property policies for pollution-related losses. Plaintiff's Proffered Facts at I, JA 251-52. To counter this prospect, reinsurer defendants entered into a written agreement to eliminate all pollution insurance products from the American market for property insurance. Entitled the "Non Marine London Market Agreement 1987," Conn. Compt. ¶ 111; Ca. Compt. ¶ 107, but signed by both American and British companies, this agreement pledges signatories to use their:

> best endeavors to ensure that all U.S.A. and Canadian exposed insurance/reinsurance business attaching on or after 1st January, 1987, will only be written where the original business includes a seepage and pollution exclusion wherever legal and applicable.

Conn. Compt. ¶ 112; Ca. Compt. ¶ 108.

This agreement, following the successful elimination of pollution coverage in the CGL market, accomplished the

conspirators' goal: the virtual elimination of all insurance products for pollution in the United States. Conn. Compt. ¶ 114; Ca. Compt. ¶ 110.[13]

By 1986, defendants had succeeded in deepening a North American insurance crisis in the market for long-tail and pollution coverage. The effects on American municipalities were particularly devastating and, as conceded by defendants, foreseeable. Hartford A-82a. As a direct result of defendants' collusive agreements, plaintiffs were unable to purchase insurance products they needed, or were forced to pay inflated prices for shrunken coverage.

### B. Proceedings and Decisions Below.

This litigation began with the filing of complaints by eight states on March 22, 1988. Ten other states filed soon thereafter.[14] Before all of the complaints had been responded to by answer or other pleading, the trial court ordered the parties to "file and serve those motions which they believe are dispositive of any claim or issue in this litigation based on the facts alleged in the complaints and other information in their possession" so long as the motions could be resolved without raising any "disputable issues of . . . fact."[15] In accordance

[13] Various defendants also sought to restrict the availability of long-tail and pollution coverage by limiting the insurance coverage for excess and umbrella insurance. Conn. Compt. ¶¶ 105-09; Ca. Compt. ¶¶ 101-05. Excess and umbrella insurance are specialized forms of insurance that are not normally offered in the admitted (regulated) market. ISO, as the trade association for admitted insurers, plays no role in the non-admitted market. Nevertheless, at the direction of primary defendants and London reinsurers, ISO generated umbrella and excess forms for use in the unregulated, non-admitted market. These forms eliminated pollution insurance and constituted yet another coercive attempt by defendants to eliminate long-tail and pollution insurance entirely from the American market. *Id.*

[14] A nineteenth state filed its complaint in 1989.

[15] Pre-Trial Order No. 2, ¶ 3a, JA 103-04 ("Motions shall not be filed that turn on disputable issues of evidentiary fact."). Further, the trial court only permitted discovery insofar as it was relevant to those motions and



with this procedure, defendants filed various motions under Rules 12(b)(1) and (6) and in part under Rule 56 of the Federal Rules of Civil Procedure asserting that the claims in plaintiffs' complaints were barred in whole or in part by the McCarran-Ferguson Act, 15 U.S.C. §§ 1101-15, the state action doctrine, plaintiffs' lack of standing, lack of subject matter jurisdiction as to the foreign defendants, the doctrine of international comity, and the failure of some plaintiffs' complaints to adequately plead a conspiracy comprising all claims. After briefing and argument, the trial court found that plaintiffs had standing, Hartford A-67a, but proceeded to dismiss the complaints on each of the other grounds urged by the defendants.

The court of appeals unanimously reversed the trial court's dismissal of the complaints. The court of appeals ruled that defendants' withholding of critical inputs, such as reinsurance, from competitors to preclude them from writing long-tail and pollution insurance products constituted a boycott within the meaning of the McCarran-Ferguson Act. Hartford A-20a-22a. Additionally, the court held that the use of unregulated foreign reinsurers to enforce the exclusion of those products from the American market, as the complaints charged, was not shielded by the McCarran-Ferguson Act. Hartford A-20a, nor by the state action doctrine. Hartford A-26a. The court of appeals also affirmed plaintiffs' standing to sue. Hartford A-17a. Further, the court found that the foreign defendants, having targeted their conspiracy on the United States, were subject to the authority of United States courts, and that the doctrine of international comity did not foreclose the exercise of that jurisdiction. Hartford A-27a-32a. Finally, the court of appeals ruled that the trial court had erred in dismissing the count from some complaints charging an over-arching conspiracy among all defendants

was not likely to raise any disputable issues of fact. Pre-Trial Order No. 2, ¶ 5, JA 105 ("Such discovery shall be further limited to matters which are not expected to raise disputable issues of fact."). Not surprisingly, no discovery was actually conducted.

without providing those plaintiffs any opportunity to amend their complaints to plead the relevant factual nexus between property and casualty insurance. Hartford A-27a.

Defendants timely filed petitions for rehearing and requests for rehearing *en banc*. These petitions and requests were denied, no judge of the circuit voting for rehearing.

### C. Proceedings in This Court.

Various groups of defendants filed timely petitions for certiorari in this Court. Those petitions sought review of the McCarran-Ferguson Act and state action holdings of the court of appeals, No. 91-1111, the international comity holding of the court of appeals, No. 91-1128, and the antitrust standing holding of the court of appeals, Nos. 91-1131 and 1146. This Court's Order of October 5, 1992, JA 308, granted a writ of certiorari in No. 91-1111 only on two McCarran-Ferguson Act questions and in No. 91- 1128 on the international comity question. To date no rulings on the petitions in Nos. 91-1131 and 1146 have been made.

## SUMMARY OF ARGUMENT

I. The court of appeals correctly found that defendants' agreements and acts to force competitor adherence to cartel decisions constitute "boycott, coercion or intimidation" within the meaning of the McCarran-Ferguson Act ("McCarran Act") and therefore are subject to judicial scrutiny under the antitrust laws. The test for a McCarran Act boycott is found in Sherman Act boycott cases. Sherman Act cases cannot be distilled to a single boycott test. Their hallmark, however, is enforcement conduct. It is the presence of enforcement conduct that distinguishes cooperative behavior, which is shielded from antitrust scrutiny by the McCarran Act, from coercive behavior, which is not.

Collective coercive conduct used as the means of eliminating competition or compelling obedience to cartel demands has long been considered a boycott. The court of appeals properly found, on the undeveloped factual record



before it, that defendants' conduct, as alleged in the complaints, falls well within this ordinary understanding of boycott. The complaints allege that defendants combined to compel competing insurers to sell only those insurance products approved by the cartel. The means of compulsion used included withholding reinsurance and statistical support services – both essential inputs for insurers. This enforcement conduct constitutes a conventional boycott as described in *St. Paul Fire & Marine Co. v. Barry*, 438 U.S. 531 (1978). The conduct is similar to that described in *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), the acknowledged genesis of the boycott exception to the McCarran Act.

Defendants self-servingly describe the complaints as alleging only agreements on forms and *voluntary* adherence to those agreements. But this description omits all mention of allegations that defendants combined to *force* competitors to adhere to cartel demands. Defendants' case description, wrongly accepted by the district court and properly rejected by the court of appeals, cannot be reconciled with the well-pleaded facts in the complaints.

Further, nothing in the text or legislative history of the McCarran Act supports defendants' argument that boycotts are limited to absolute or discriminatory refusals to deal. Supreme Court cases are also to the contrary. It is the existence, and not the extent, of coercion that determines whether conduct constitutes "boycott, coercion or intimidation." Here, defendants' refusals to offer reinsurance and statistical support services were the means of eliminating competition from insurers that would otherwise sell competing coverage products, and constitute boycott, coercion or intimidation.

Subjecting defendants' conduct to antitrust review will not impair the necessary operations of the insurance industry. Applying antitrust scrutiny to agreements to prevent competitors from offering competing products in no way threatens the ability of primary insurers to confer with reinsurers about their own products, or to engage in other normal business activity. Indeed, in enacting the McCarran Act, Congress

distinguished precisely between voluntary agreements on policy terms – which are immunized if adequately regulated by the state – and combinations designed to force unwilling competitors to adhere to terms – which are not immune. Congress preserved antitrust scrutiny of the latter to prevent members of the insurance industry from installing with impunity a private system of government affording themselves great economic advantage without regard for the public good.

The conduct challenged in these cases is precisely the evil addressed by the McCarran Act's boycott provision. Defendants' enforcement conduct is subject to antitrust review in the federal courts.

II. Section 2(b) of the McCarran Act establishes a limited antitrust immunity for the business of insurance "to the extent" regulated by the states. Unregulated conduct does not qualify for McCarran immunity. The court of appeals correctly concluded that the challenged conduct of the London-based reinsurers is not regulated within the meaning of section 2(b) of the McCarran Act. Further, none of the reinsurers' relevant acts are regulated within the plain meaning of section 2(b) because state insurance laws do not reach their conduct. This unregulated conduct is subject to judicial scrutiny under the antitrust laws.

As a matter of mainstream conspiracy law, all conspirators are liable for the antitrust injuries that flow from conduct to which they agree. Since all conspirators in these cases agreed to reinsurers' unregulated conduct, all are liable for the antitrust injuries that this conduct creates. Any other ruling would nullify the plain language of the McCarran Act that exempts conduct only "to the extent" regulated by state law. Moreover, any other ruling would create a regulatory void, undercutting the "cooperative federalism" of the McCarran Act.

Application of established conspiracy law to defendants' conduct in these cases would strengthen state regulatory schemes by foreclosing opportunities to evade them. Far from impinging on state interests in regulating insurance activity, this rule would enable States to rely upon competition to supplement insurance regulation.



Conduct subject to antitrust scrutiny is not necessarily unlawful. Insurance entities should have no difficulty in discerning the difference between lawful agreements regarding the purchase of reinsurance and unlawful agreements to withhold reinsurance and other essential inputs from competitors.

III. When additional antitrust injury flows from regulated conduct alone, a separate question of McCarran Act immunity arises. Under analogous Supreme Court precedent, McCarran Act immunity is inapplicable where, as here, regulated conduct furthers an unlawful conspiracy that relies upon unregulated acts.

This Court has easily found the labor exemption from the antitrust laws inapplicable when nominally exempt agreements undercut the purpose of the exemption. The logic of the labor cases applies even more strongly in the insurance context. When insurers act jointly within the context of state-authorized processes, they act consistently not only with state law, but also with the purposes of the McCarran exemption. In the present cases, insurers and reinsurers entered into unregulated, anticompetitive agreements to impose cartel terms on competitors. In doing so, they moved beyond the ambit of state regulation and crossed the line drawn by the McCarran Act's exemption. All defendants' conduct should be subject to antitrust review.

## ARGUMENT

### I. THE COMPLAINTS, WHICH ALLEGE CONDUCT TO FORCE NON-CONSPIRING INSURERS TO ADHERE TO CARTEL TERMS, PLEAD "ACTS OR AGREEMENTS OF BOYCOTT, COERCION OR INTIMIDATION" WITHIN THE MEANING OF THE MCCARRAN-FERGUSON ACT.

Under the McCarran-Ferguson Act ("McCarran Act"), 15 U.S.C. §§ 1011-15, the federal courts retain the authority to scrutinize anticompetitive conduct within the insurance business when that conduct constitutes "boycott, coercion or intimidation". 15 U.S.C. § 1013(b). Without judicial review of this conduct, members of the insurance industry may with

impunity install a private system of government affording themselves great economic advantage without regard for the public good. *See, e.g.*, 91 Cong. Rec. 1480, 1485 (1945) (remarks of Senator O'Mahoney), JA 221-23, ¶¶ 13, 16.

The complaints allege just such an effort. Together, defendant insurers and reinsurers determined neither what the commercial general liability insurance market would bear, nor simply what terms and conditions they might offer to meet existing demand. Instead, defendants defined what insurance products they wanted to sell and then eliminated the means by which their competitors could sell alternatives.

The withholding of trade relations for the purpose of pressuring competitors to accede to cartel demands has long been considered a boycott. *St. Paul Fire & Marine Ins. Co. v. Barry*, 438 U.S. 531 (1978). Defendants' conduct is a boycott under this conventional definition. Far from simply standardizing the terms under which some insurance products could be offered, defendants combined to force competitors to adhere to their cartel's demands. By choking off access to reinsurance and statistical support, inputs essential for writing insurance, defendants foreclosed to competitors and consumers alike the opportunity to sell or buy insurance products other than those approved by the cartel.

The court of appeals properly found this enforcement conduct to be "boycott, coercion or intimidation" within the meaning of the McCarran Act. Its decision, well within the traditional understanding of boycott articulated by this Court, should be upheld.

### A. The narrow antitrust exemption provided by the McCarran Act does not extend to boycott, coercion or intimidation.

Before *United States v. South-Eastern Underwriters Assn.*, 322 U.S. 533 (1944) ("*SEUA*"), the insurance industry enjoyed a blanket exemption from the federal antitrust laws. The exemption evaporated, however, when this Court decided that the business of insurance is interstate commerce. *Id.* at 553.



Congress then enacted the McCarran Act. Congress' primary purpose in doing so was to affirm the power of the states to tax and regulate the business of insurance, notwithstanding its delineation as interstate commerce. *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 217-18 (1979). Legislating in the wake of *SEUA*, Congress also enacted the McCarran Act to redefine the contours of the antitrust exemption applicable to the insurance industry. *Royal Drug*, 440 U.S. at 218-19.

The antitrust exemption set out in the McCarran Act is, by its own terms, limited. Not all insurance industry conduct qualifies for the exemption.[16] Moreover, a "broad and unqualified" exception to the exemption makes the antitrust laws applicable to *any* act or agreement of boycott, coercion or intimidation. *Barry*, 438 U.S. at 549-50.

The McCarran Act thus embodies "a legislative rejection of the concept that the insurance industry is outside the scope of the antitrust laws. . . . " *Royal Drug*, 440 U.S. at 220. The industry is afforded an antitrust exemption, but this exemption is limited by the plain meaning of the language Congress used to establish the exemption and to carve out an exception for "boycott, coercion, or intimidation."[17]

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[16] The McCarran Act exempts from antitrust scrutiny the business of insurance alone, and then only "to the extent" regulated by State law. 15 U.S.C. § 1012(b). As is shown in Part II of this argument, defendants fail even to qualify for this limited exemption because their conduct was not regulated by the states.

[17] Ordinary rules of statutory construction require that this limited exemption be "narrowly construed." *Royal Drug*, 440 U.S. at 231; *accord Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 126 (1982). Faithful to these rules, every Supreme Court decision on McCarran in the last thirty years has circumscribed the reach of the exemption. *Id.* (narrowing the "business of insurance" test); *Royal Drug*, 440 U.S. 205 (narrowing the "business of insurance" test); *Barry*, 438 U.S. 531 (narrowing the exemption by broadly defining the boycott exception); *FTC v. Travelers Health Ass'n.*, 362 U.S. 293 (1960) (narrowing the state regulation test); *cf. SEC v. National Securities, Inc.*, 393 U.S. 453 (1969) (narrowing the "business of insurance" test).

The boycott exception states: "*Nothing* contained in [the McCarran Act] shall render the said Sherman Act inapplicable to *any* agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation." 15 U.S.C. § 1013(b) (emphasis added). No limiting language appears in the text. If the industry conduct is a boycott, or if it is coercive, or if it is intimidating, the McCarran Act does not shield it from antitrust review.

**B. Defendants' conduct constitutes boycott, coercion or intimidation within the meaning of the McCarran Act.**

**1. At a minimum, the term boycott as used in the McCarran Act includes concerted refusals to deal designed to prevent firms from competing effectively and to force competitors to accede to cartel demands.**

In the only instance in which it has construed the boycott exception in the McCarran Act, this Court relied on Sherman Act boycott cases, finding specifically that Congress intended the McCarran Act to be read in light of those cases. *Barry*, 438 U.S. at 541 (In enacting the McCarran boycott exception, "Congress . . . employed terminology that evokes a tradition of meaning, as elaborated in the body of decisions interpreting the Sherman Act. It may be assumed, in the absence of indications to the contrary, that Congress intended this language to be read in light of that tradition."). The test for a McCarran Act boycott is, therefore, found in Sherman Act cases.[18]

[18] In their opening brief, defendants entirely disregard this Court's holding in *Barry* that Sherman Act cases determine the meaning of "boycott, coercion or intimidation."



Sherman Act boycott cases cannot be distilled to a single boycott test. *Id.* at 541-43.[19] What they have in common, however, is collective coercive conduct used as the means of eliminating competition or compelling obedience to cartel demands.

Thus, conduct constituting private enforcement of industry rules and practices is a boycott. *Id.* at 548-49. On this point, the Court has been unanimous. *Compare* the majority ruling in *Barry, id.*, at 541 ("The generic concept of boycott refers to a method of pressuring a party with whom one has a dispute, by withholding or enlisting others to withhold patronage or services from the target.") *with* the dissent in *Barry, id.* (Stewart, J. dissenting) ("[T]he 'boycott, coercion, or intimidation' provision is most fairly read as referring to . . . attempts by members of the insurance business to force other members to follow the industry's private rules and practices.")

Similarly, conduct designed to deprive competitors of an essential input or the means of effective competition is a boycott. *Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*, 472 U.S. 284, 294 (1985) (the term boycott includes "joint efforts by a firm or firms to disadvantage competitors by 'either directly denying or persuading or coercing suppliers or customers to deny relationships the competitors need in the competitive struggle.' "); *see also Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959); *Associated Press v. United States*, 326 U.S. 1 (1945).

When conspirators use concerted refusals to deal as the means of forcing others to conform competitive practices to conspiratorial dictates, the conduct has always been viewed as a boycott. *Barry*, 438 U.S. at 544-45. *See, e.g., FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 431 (1990) (message of boycotting conduct is, "We will not do business until you do what we ask"); *Fashion Originator's*

[19] "[B]oycotts are not a unitary phenomenon" and there exists no single definition of the term. *Barry*, 438 U.S. at 543 (quoting P. Areeda, *Antitrust Analysis* 381 (2d ed. 1974)).

*Guild v. FTC*, 312 U.S. 457 (1941); *Eastern States Retail Lumber Dealers Ass'n v. United States*, 234 U.S. 600, 612-13 (1914); *In re Workers Comp. Ins. Antitrust Litig.*, 867 F.2d 1552 (8th Cir.), *cert. denied*, 492 U.S. 920 (1989).

Enforcement conduct is, therefore, the hallmark of a boycott. Enforcement conduct separates a boycott from a mere agreement to restrict output or to fix prices or other terms.[20] The distinction is between cooperation, on the one hand, and coercion, on the other. *Barry*, 438 U.S. at 549. The basis for this distinction is found in the very purpose of the boycott exception, which "was viewed by the Act's proponents as an important safeguard against the danger that insurance companies might take advantage of purely permissive state legislation to establish monopolies and enter into restrictive agreements *falling outside the realm of state-supervised cooperative action*." *Id.* at 547 (emphasis added).

Enforcement conduct is the "larger evil" Congress made subject to antitrust scrutiny. *Id.* at 547. Congress expected the antitrust laws to apply to coercive conduct and private systems of regulation. Defendants in these cases can expect no less.

**2. The complaints allege concerted refusals to deal designed to prevent firms from competing effectively, to force competitors to accede to cartel decisions and to deny consumers access to particular products.**

Plaintiffs have alleged conduct falling well within the ordinary meaning of boycott. The complaints allege that

[20] The exchange between the majority and dissent in *Barry* affirms this conclusion. The *Barry* dissent argued that reliance on Sherman Act cases to define McCarran Act boycotts would read section 3(b) too broadly. *Barry*, 438 U.S. at 556. The *Barry* majority rejected this argument, noting that not all Sherman Act violations are boycotts. *Barry*, 438 U.S. at 545 n.18. Among the non-boycott conduct is "price-fixing, in the absence of additional enforcement activity." *Id.* In other words, enforcement conduct is what distinguishes a mere price-fixing agreement from a boycott.



primary insurer defendants attempted to persuade their competitors to agree voluntarily to change the forms on which certain insurance was offered in order to limit competition for commercial general liability insurance. When primary insurer defendants were unable to get voluntary acquiescence, they forced capitulation. They enlisted reinsurers to withhold reinsurance, a key input needed by competing, non-conspiring primary insurers in United States markets. At the behest of the four primary defendants, the reinsurers conspired to refuse to deal with insurers in the United States who offered the insurance products primary insurers wanted to ban. The pressure created by defendants' concerted acts forced recalcitrant insurers to accede to the defendants' private demand – that all members of the industry stop selling the insurance products the cartel wanted to ban from the market.

Defendants further compelled compliance with their demand by withdrawing another critical input that recalcitrant insurers would need to compete effectively: statistical support for the products banned by the cartel. As a result, the boycotted insurers were unable to sell the banned products in the market, causing injury to consumers who wanted to buy them.

These allegations state a classic boycott. They describe concerted refusals to deal that had the purpose and effect of forcing nonconspiring insurers to acquiesce to cartel decisions and denying consumers access to desired insurance coverage. These refusals are indistinguishable from the conduct that was the acknowledged genesis of the boycott exception to the McCarran Act, the conduct described by this Court in *SEUA*, 322 U.S. at 535.

In *SEUA*, the conspirators fixed premiums. This conduct alone did not constitute a boycott. But the conspirators also acted to ensure that non-conspiring competitors adhered to the fixed prices. *Id.*[21] To that end, conspirators took a series

[21] Defendants are flatly wrong when they assert that the "object of the conspiracy [in *SEUA*] was to exclude all non-members from participating in this business." Hartford Br. 35. The object of the coercion was to "force non-member insurance companies into the conspiracies." *SEUA*,

of coercive steps, including the denial of reinsurance to insurers who refused to accept the conspirators' price terms. *Id.*[22] On the basis of this enforcement conduct, the Court found a boycott in *SEUA*.

Similarly, in these cases, defendants sought to fix the products to be sold in the primary insurance markets. Plaintiffs do not allege that voluntary agreements on fixed terms of coverage constitute a boycott. Conspirators, however, also acted to ensure that non-conspiring competitors adhered to the fixed terms. To that end, defendants took a series of coercive steps, including the denial of reinsurance for CGL and property insurance and withdrawal of statistical and rate-making support for excluded products. This enforcement conduct, precisely like the conduct in *SEUA*, is a classic boycott.

The complaints thus allege conduct that fits precisely within the "tradition of meaning" of a boycott. *Barry*, 438 U.S. at 541. They assert efforts by private firms to combine not only for product-fixing purposes, but also to coerce adherence to the agreement to use only the products so fixed. Even the 1944 National Association of Insurance Commissioners ("NAIC") Memorandum of Explanation on the McCarran Act understands this enforcement conduct to be subject to the antitrust laws. 90 Cong. Rec. A4407 (1944), JA 216-17, ¶ 2. ("No twilight zone is permitted, and where any group of insurers seek [sic] to act in concert to *enforce* so-called

322 U.S. at 535. That is, the purpose was to require adherence to the agreement as to the price terms on which insurance would be sold.

[22] The witholding of reinsurance in *SEUA* was a "principal instrument utilized to compel adherence to private rate-fixing agreements. . . . [It was] used to coerce the companies directly. . . . The heavy club used by the board companies to police their rating agreements and to obtain adherence of competitors to such agreements is reinsurance." *Joint Hearing Before Subcomms. of the Committees on the Judiciary on S. 1362, et al.*, 78th Cong., 1st Sess., Part 2, 48 (1943) (testimony of Francis Biddle, Attorney General of the United States).



advisory rates, the antitrust laws will not be inapplicable.") (emphasis added.)[23]

Defendants cannot prevail on the law and so they seek to recast the facts. They "reduce" the allegations in the complaints to two sets of unrelated agreements – a horizontal agreement in which a group of primary insurers get together to develop standardized insurance policy forms and an entirely separate horizontal agreement in which reinsurers agree on the reinsurance to offer. Self-servingly, defendants describe additional conduct as voluntary adherence to those agreements. Hartford Br. 38. This description omits all mention of enforcement conduct, and cannot be reconciled with the well-pleaded facts in the complaints[24] or with the obligation to draw reasonable inferences in plaintiffs' favor at this early stage of the proceeding.[25]

Defendants must deny the interrelationship between the conduct of the primary insurers and reinsurers because that

[23] "The views of the NAIC are particularly significant because the Act ultimately passed was based in large part on the NAIC bill." *Royal Drug*, 440 U.S. at 221 (citing 91 Cong. Rec. 483 (1945) (remarks of Senator O'Mahoney)).

[24] Defendants' Banfield Affidavit and State-by-State Appendix, portions of which are reproduced in the Joint Appendix at 113 - 215, are wholly irrelevant to the boycott issue. These documents merely provide information on the process for obtaining approval of policy forms in some states. They do not address defendants' acts of boycott: their threatened withholding of reinsurance, their actual withholding of reinsurance and their discontinuance of statistical support. Further, any suggestion in defendants' documents that plaintiff States disfavor competition in the sale of insurance is refuted by States' Regulatory Appendix which demonstrates, among other things, that states favor competition in the provision of insurance coverages. *See* JA 225 *et seq.; see also infra* note 53.

[25] This case remains in its procedural infancy. *See supra* notes 1 and 15 and accompanying text. The district court permitted no discovery of disputable facts; no discovery has been taken. *Id.* Moreover, the boycott issue now before this Court arises from a motion under Fed. R. Civ. P. 12(b)(6). *Id.* At this early stage in the proceeding, all reasonable inferences that defendants engaged in coercive conduct to force competitors to adhere

connection defeats their boycott argument. Only if new forms were developed and used voluntarily, without coercive interference, can defendants sustain the fiction that all of their conduct is reducible to mere agreements on terms. Only if the reinsurers acted in benign isolation from the cartel demands of the primary insurers can defendants support their contention that they innocently withdrew reinsurance and statistical support "in accordance with [their] protected agreements," Hartford Br. 38, and not, as alleged in the complaints, as an unlawful means of compelling competitor acquiescence.

This Court has long cautioned against viewing related conduct in isolation. *United States v. Patten*, 226 U.S. 525, 544 (1913) ("[T]he character and effect of a conspiracy are not to be judged by dismembering it and viewing its separate parts, but only by looking at it as a whole."); *Continental Ore Co. v. Union Carbide and Carbon Corp.*, 370 U.S. 690, 707 (1962). Moreover, "[i]n cases such as this, plaintiffs should be given the full benefit of their proof without tightly compartmentalizing the various factual components and wiping the slate clean after the scrutiny of each." *Id.*

The court of appeals refused defendants' invitation to reduce the allegations of the complaints and dismember them into separate parts.[26] Properly viewing the complaints as a whole, the Ninth Circuit found "much more" than a simple agreement on terms; it found enforcement conduct left unprotected by the exemption afforded the insurance industry under the McCarran Act. The court of appeals' boycott ruling, based on application of settled law to facts properly understood, should be upheld.

to cartel demands must be drawn in the plaintiffs' favor. *Summit Health Ltd. v. Pinhas*, 111 S. Ct. 1842, 1845 (1991).

[26] Judge Noonan recounted the various activity undertaken by defendants and rejected defendants' contention that their conduct was not interrelated. Hartford A-21a. Thus, "Hartford and the other primary defendants . . . enlisted the reinsurers to compel capitulation by ISO and the insurers who refused to go along with the Hartford demands." Hartford A-22a.



### 3. Defendants' definition of boycott lacks support in the McCarran Act's text and legislative history and is contradicted by case law.

Defendants acknowledge that they engage in a boycott when they use enforcement activity to compel adherence to cartel demands. Hartford Br. 28-29. To avoid application of this rule to their own conduct, however, defendants redefine enforcement activity to exclude all coercive conduct except that constituting "absolute refusals to deal on any terms or discriminatory activity." Hartford Br. 31-32. This alluringly simple formula has no basis in the text or legislative history of the McCarran Act. Further, it is contradicted by case law which finds a boycott when a refusal to deal is neither absolute nor discriminatory.

As already shown, nothing in the text of the McCarran Act limits the phrase "boycott, coercion or intimidation."[27] 15 U.S.C. § 1013(b). Not only are "any" acts or agreements of boycott excepted from the antitrust exemption; "any" acts and agreements of coercion and intimidation are excepted as well. Yet defendants argue that the phrase is limited. They insist that the term does not reach all coercive marketplace activity, but only a small subset of that activity. In short, they argue that most coercion is not coercion for the purposes of the Act. But the "broad and unqualified" text of the Act devastates this argument. *Barry*, 438 U.S. at 549-50.

Like the text of the exception itself, the McCarran Act's legislative history refers to the boycott exception in broad and unqualified terms.[28] The McCarran Act preserves for antitrust scrutiny "*all* steps by which small groups have attempted to establish themselves in control in the great interstate and international business of insurance." *Id.* at 548 (emphasis added), citing 91 Cong. Rec. 1485 (1945) (remarks of Senator O'Mahoney), JA 223 ¶ 16. Nothing in the text or legislative

[27] *See supra* pp. 16-18.

[28] Portions of the legislative history relevant to the scope of the McCarran Act's limited antitrust exemption are set out in JA 216-24.

history of the McCarran Act justifies limiting "boycott, coercion or intimidation," as defendants suggest, to a subset of its own terms.[29]

In all their prior briefs, defendants argued that only absolute refusals to deal qualify as boycotts. Defendants cite *Barry* as support for this notion. But defendants mistake the *Barry* Court's statement of facts for its holding. The *Barry* Court did not hold that an absolute refusal to deal is a necessary element of boycott, coercion or intimidation. It held that boycotts are not a unitary phenomenon and that efforts to force adherence to the terms of an agreement is a boycott. *Id.* at 543-45.

Apparently recognizing the numerous cases and substantial authority that find a boycott in the absence of an absolute refusal to deal,[30] defendants now acknowledge that an absolute refusal to deal is not "an invariable or talismanic element

[29] Precisely opposite defendants' notion,

> [t]here has never been any doubt . . . that private agreements by which these rates were *enforced* were violations and are violations of the antitrust laws. There is nothing in the conference report that relieves insurance companies from the prohibition of the antitrust law, because there has been written back into the bill language which was taken out by the House which would have exempted agreements from the prohibition of the antitrust law. Therefore *any* attempt by a small group of insurance companies to enter into an agreement by which they would penalize any person or any business which was attempting to do business in the insurance field in a way that was disapproved by them, would be absolutely prohibited by this provision.

91 Cong. Rec. 1480 (1945) (remarks of Senator O'Mahoney), JA 221-22, ¶ 13 (emphasis added).

[30] "[T]he large majority of cases have held that an absolute refusal to deal is not required to bring the conduct within [the McCarran Act boycott exemption]; a partial or conditional refusal to deal, if it is designed to coerce the target to conform to certain conduct, will still be deemed a 'boycott.' " 9 E. Kintner & J. Bauer, *Federal Antitrust Law* § 70.12 at 245-46. *See, e.g., FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 458 (1986), in which this Court, citing *Barry*, found a boycott based on evidence of "a concerted refusal to deal on particular terms" whose purpose and effect was to force insurers to change their competitive behavior. *See also Northwest Wholesale Stationers*, 472 U.S. at 295 n.6 (recognizing that partial refusals to deal may have the same effects as absolute refusals to deal); *Virginia Academy of Clinical Psychologists v. Blue Shield of Va.*, 624 F.2d 476, 484 (4th Cir. 1980), *cert. denied*, 450 U.S. 916 (1981); *Proctor v. State Farm Mut. Auto Ins. Co.*, 561 F.2d 262, 274-75 (D.C. Cir. 1977), *vacated on other grounds*, 440 U.S. 942 (1979); *In re Workers Comp. Ins. Antitrust Litig.*, 574 F. Supp. 525, 535 (D. Minn. 1983); *Trident Neuro-Imaging Lab. v. Blue Cross*, 568 F. Supp. 1474, 1479 (D.S.C. 1983); *Nurse Midwifery Assoc. v. Hibbett*, 549 F. Supp. 1185, 1191 (M.D. Tenn. 1982); *Workman v. State Farm Mut. Auto. Ins. Co.*, 520 F. Supp. 610, 623 (N.D. Cal. 1981); *Hoffman v. Delta Dental Plan of Minnesota*, 517 F. Supp. 564, 572 (D. Minn. 1981); *California League of Indep. Ins. Producers v. Aetna Cas. & Sur. Co.*, 179 F. Supp. 65, 66 (N.D. Cal. 1959).



of a boycott" but "merely a probative factor." Hartford Br. 32 n.14.[31] Further, defendants now redefine boycott to include both absolute refusals to deal and discriminatory refusals. Defendants cite not a single case that supports their still constricted definition. Supreme Court cases are to the contrary.

In *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.*, 364 U.S. 656 (1961), manufacturers of gas burners agreed on which products they wanted to sell. To force market adherence to this agreement, the manufacturers enlisted the aid of gas utilities, who agreed to provide natural gas only to customers who used a "certified" gas burner. The utilities were willing to deal on particular terms (only when certified burners were used) and in a non-discriminatory manner (all

[31] The *Barry* Court found the "absoluteness" of a refusal to deal to be a sufficient probative factor of a boycott where, as in that case, consumers were the target. Where, as in these cases, competitors rather than consumers are the direct target of the boycott, evidence of an absolute refusal to deal is not a necessary probative factor. *See* Brief for the United States as Amicus Curiae on Petition for a Writ of Certiorari at 12; *see also* 9 E. Kintner & J. Bauer, *Federal Antitrust Law*, § 70.12 at 245-46.

customers accepting the product limitation could purchase natural gas on equal terms). Nevertheless, their conduct constituted a boycott.

Similarly, in *United States v. General Motors*, 384 U.S. 127, 143 (1966), some dealers of General Motors cars agreed not to deal with discounters and "enlist[ed] the aid of General Motors" to enforce their agreement. General Motors agreed "to bring wayward dealers into line" by demanding adherence to the location clause common to all dealers' franchise contracts. Citing the same cases relied upon by the Court in *Barry*, the Court in *General Motors* found a boycott based on General Motors' refusal to deal, even though that refusal was neither absolute nor discriminatory. *General Motors*, 384 U.S. at 145-48. Where private entities combine to force recalcitrant competitors to acquiesce, a boycott has been alleged. *Id.*

Defendants in these cases acted no differently than did defendants in *Radiant Burners* and *General Motors*. Primary defendants, like the manufacturers in *Radiant Burners* and the dealers in *General Motors*, enlisted the aid of reinsurer defendants to bring recalcitrant competitors in line. Reinsurer defendants, like the utilities in *Radiant Burners* and the producer in *General Motors*, took the necessary steps to do so. There was no threat of an absolute refusal to deal or discrimination. There was simply enforcement conduct, withdrawal of reinsurance and statistical support, to ensure adherence to a private system of regulation erected to cripple competition.

Thus, it is the existence, and not the extent, of coercion that determines whether conduct constitutes "boycott, coercion or intimidation." Professors Areeda and Hovenkamp, reviewing the very cases now before this Court, confirm this conclusion:

> The Ninth Circuit [held] correctly that 'boycott' encompasses a conditional refusal to deal 'except on the terms demanded. The evil of a boycott is not its absolute character but the use of the economic power of a third party to force the boycott victim to agree to the boycott beneficiary's terms.'



P. Areeda and H. Hovenkamp, *Antitrust Law*, ¶ 210.2 at 124 (Supp. 1992).

As used in the McCarran Act, "boycott, coercion or intimidation" means enforcement activity designed to compel adherence to cartel demands. The Act does not distinguish between concerted conduct that, on the one hand, destroys competitors and concerted conduct that, on the other, forces competitors to obey the cartel's demands. It does not matter whether the enforcement mechanism is absolute or partial, discriminatory or evenhanded. What matters is whether private entities act in concert to force their economic will on others.[32] Defendants' refusals to offer reinsurance and statistical support, used as a means of eliminating competition from insurers that would otherwise persist in selling long-tail and pollution coverage, constitute boycott, coercion or intimidation.

## C. ANTITRUST SCRUTINY OF DEFENDANTS' COERCIVE CONDUCT WILL NOT UPSET THE NECESSARY OPERATION OF THE INSURANCE INDUSTRY.

Defendants complain that shining the light of antitrust scrutiny on their conduct will impair the "historic and necessary" ability of insurers to confer with reinsurers and agree on the terms of primary insurance. Hartford Br. 40. But it is one thing for primary insurers to confer and agree with reinsurers as to terms of reinsurance for their own policies, and quite another to confer and agree on a course of action designed to prevent competitors from competing on their own terms.

[32] If a group of conspirators seek to eliminate competition from a single product offered by their competitors, they need go no further than withholding one essential component of that product. But under defendants' definition of boycott, this would not constitute a boycott. Defendants offer no defensible economic reason to distinguish between conditional, absolute and partial refusals to deal where, as here, competitors are the direct target of the boycott. No defensible distinction exists.

Applying antitrust scrutiny to the latter agreement in no way threatens the former.[33]

Defendants further claim that their conduct should be excused because policy form "standardization protects consumers and their agents and brokers from facing an unintelligible array of insurance forms. . . . " Hartford Br. 91-1111 at 3. But defendants went beyond mere product standardization; they engaged in enforcement conduct. Moreover, defendants fail to explain how antitrust review of their enforcement conduct would create the "unintelligible array" they fear.[34]

Congress enacted the boycott exception to leave "absolutely" unprotected "any attempt by a small group of insurance companies to enter into an agreement by which they would penalize any person or any business which is attempting to do business in the insurance industry in any way that was disapproved by them." 91 Cong. Rec. 1480 (1945) (remarks of Senator O'Mahoney), JA 221-22, ¶ 13.[35] In doing

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[33] Moreover, reinsurance transactions are not likely to be inhibited by antitrust scrutiny at all. Reinsurers have historically conducted their affairs subject to antitrust rules. N. David Thompson, *Critical Issues of the Eighties: How Trends in Reinsurance Will Affect Legal, Legislative, and Regulatory Actions*, 16 Forum 1038, 1055 (1980-81). Mr. Thompson is president and chief executive officer of Defendant North American Reinsurance Corp. *See also* Havens & Theisen, *The Application of the United States and the EEC's Antitrust Laws to Reinsurance Pooling Arrangements*, 54 Antitrust L.J. 1299 (1986). *See also* references cited *supra* note 7.

[34] *See supra* note 9. In addition, it is the regulatory function of the states, not the private insurers, to protect consumers from incidental difficulties inherent in competitive markets.

[35] Defendants' only escape from antitrust scrutiny is to describe their conduct antiseptically as mere "implementation" of an agreement on terms. Hartford Br. 45. By this choice of words, defendants attempt, first, to divest their conduct of all coercive taint and, second, to bolster their claim that these cases are about nothing more than economic exigencies that are the "natural effect of" immunized, horizontal agreements on terms. *Id.* But the allegations in the complaint are not about unrelated ordinary-course-of business arrangements against which other insurers found it difficult or expensive to compete. They are about the withdrawal of reinsurance and statistical support as the means of enforcing adherence to the demands of conspirators. As Judge Noonan correctly observed, "when 'the economic exigencies' are produced by conspirators who refuse to supply reinsurance if the unwilling insurer does not agree, a boycott is in effect and is being implemented." Hartford A-25a.



so, Congress carefully distinguished voluntary agreements on policy terms – which could claim antitrust immunity if adequately regulated by the state – from combinations designed to force unwilling competitors to adhere to terms through the concerted denial of necessary trade relationships – which were expressly denied immunity. *Barry*, 438 U.S. at 547-50. The McCarran Act enables states to permit voluntary cooperative conduct, but it in no way authorizes coercive conduct.[36]

The ability of defendants to make unilateral decisions to withdraw reinsurance or statistical support is, finally, "beside the point." *General Motors*, 384 U.S. at 140. The point is that defendants engaged in a concerted process that "can by no stretch of the imagination be described as 'unilateral' or merely 'parallel'." *Id.* They acted jointly to eliminate the means by which competitors could persist in selling long-tail and pollution coverage. "What resulted was a fabric interwoven by many strands of joint action to eliminate [competitors] from participation in the market, to inhibit the free choice of [competitors] to select their own methods of trade and to provide multilateral surveillance and enforcement." *Id.*

The conduct challenged in these cases constitutes exactly the vice that the boycott exception sought to preclude. *Barry*, 438 U.S. at 548. Application of the antitrust laws to defendants' conduct would not undermine the purposes of the McCarran Act. To the contrary, it would give meaning to the safeguard provided by the Act's boycott provision. Defendants' enforcement conduct is subject to antitrust review.

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[36] While defendants cite legislative history attesting to the need for cooperative conduct in the business of insurance, defendants completely ignore the legislative history concerning the boycott exception. *See* JA 216-24 (reproducing relevant portions of the McCarran Act's legislative history).

## II. REGARDLESS OF WHETHER IT CONSTITUTED BOYCOTT, COERCION OR INTIMIDATION, DEFENDANTS' CONDUCT IS SUBJECT TO ANTITRUST REVIEW BECAUSE IT IS NOT "REGULATED BY STATE LAW".

The Ninth Circuit found that the challenged conduct of the London-based reinsurers is not regulated within the meaning of section 2(b), and, therefore, not exempt from antitrust scrutiny.[37] These defendants are liable for all antitrust injury that flows from their unregulated conduct. Under established principles of conspiracy law, all co-conspirators are also liable for the antitrust injury that flows from the reinsurers' unregulated conduct. Thus, a second and alternative basis for exposing defendants' conduct to antitrust review is not, as defendants assert, that they have forfeited the exemption, but rather, that defendants' conduct was outside the scope of the exemption in the first instance.

### A. The McCarran Act exempts only regulated conduct.

Section 2(b) of the McCarran Act, 15 U.S.C. § 1012(b), establishes a limited antitrust immunity for the business of insurance "to the extent" regulated by the States.[38] None of the reinsurers' relevant acts are regulated within the plain meaning of section 2(b) of the McCarran Act. Such regulation requires, *inter alia*, *both* a state insurance regulatory law purporting to regulate the particular activities at issue, *FTC v.*

[37] Defendants currently "believe" that "*all* of the defendants, foreign and domestic, are entitled to McCarran immunity . . . . " Hartford Br. 18 n.8. This belief is inconsistent with industry statements confirming that no reinsurer conduct is exempted from antitrust scrutiny under the McCarran Act. *See supra* note 7. The States contend that the conduct of *all* reinsurers directed at the North American market fails to qualify for the McCarran Act exemption.

[38] Ordinary rules of statutory construction require that this limited exemption be narrowly construed. *See supra* notes 16-17 and accompanying text.



*National Casualty Co.*, 357 U.S. 560 (1958), *and* the means through which the state can assert direct control, within its own boundaries, over the regulated parties. *Compare id. with Travelers Health Ass'n v. FTC*, 298 F.2d 820, 823 (8th Cir. 1962), *on remand from* 362 U.S. 293, 297 (1960). In these cases, neither requirement is met.

State insurance regulatory laws do not purport to regulate the activities of the reinsurers in these cases. Indeed, N. David Thompson, the president and chief executive officer of defendant North American Reinsurance Corp. has admitted in a non-litigation context that reinsurance is not sufficiently regulated for McCarran Act exemption to apply.[39] N. David Thompson, *Critical Issues of the Eighties: How Trends in Reinsurance Will Affect Legal, Legislative, and Regulatory Actions*, 16 Forum 1038, 1055 (1980-1981). The 1989 American Bar Association Report of the Commission to Improve the Liability Insurance System, at 25, in examining this very issue, likewise concludes that reinsurance is effectively unregulated. *Accord*, Havens and Theisen, *The Application of United States and EEC Antitrust Laws to Reinsurance and Insurance Pooling Arrangements*, 54 Antitrust L.J. 1299, 1307-8 (1986).[40] Even in their own brief to this Court, Hartford Br. 6-8, defendants acknowledge that the focus of state

[39] The reasons for the limited reach of state regulation of international reinsurance transactions are apparent in legislative history of the McCarran Act previously relied on by this Court. *FTC v. Travelers Health Ass'n*, 362 U.S. 293, 298-99, 302 (1960). At the time of the McCarran Act's passage, state insurance regulators were believed to have no jurisdiction over international insurance transactions. House Comm. on the Judiciary, *Expressing the Intent of the Congress with Reference to the Regulation of the Business of Insurance*, H.R. Rep. No. 143, 79th Cong., 1st Sess., at 3 (1945), *reprinted in* 1945 U.S. Code Cong. Serv. 670, 671-72; *State Board of Insurance v. Todd Shipyards Corp.*, 370 U.S. 452, 456 (1962); 1J. Atwood & K. Brewster, *Antitrust and American Business Abroad*, 78-79 (2d ed. 1981). Since that time, state insurance regulatory laws generally have not attempted to reach such transactions.

[40] Charles W. Havens, III is the former president of defendant Reinsurance Association of America.

insurance regulators lies not with reinsurance, but in the regulation of the policy relationship between direct insurers and business or individual consumers of insurance services.

Reinsurance contracts, unlike direct insurance policies, ordinarily need not be filed with state insurance departments for approval. The states do not regulate the sale of reinsurance in general or specifically with regard to form, type of product, conditions of sale or how and to whom sold. *See* States' Reg. App., JA 225-50, ¶ E. The rate-making statutes of some states, under which forms of coverage are reviewed expressly exclude reinsurance. *See, e.g.*, California's McBride-Grunsky Act, Cal. Ins. Code § 1851(a), JA 227, ¶ C; Conn. Gen. Stat. § 38-28, JA 234. The Unfair Insurance Practices Acts of many states do not apply to the foreign reinsurers' relevant conduct. *E.g.*, New York Ins. Law §§ 1101(b)(2), 2402(a), JA 247-49. In any event, they merely mimic the McCarran Act prohibition on boycotts, coercion or intimidation. This prohibitory language is not sufficient to constitute state regulation within the meaning of section 2(b). The record in these cases, including the published words of reinsurer defendants themselves, demonstrate that the conduct of the reinsurer defendants was not regulated by any state within the meaning of section 2(b), and remains subject to the federal antitrust laws.

The Ninth Circuit ruling found only the conduct of London-based defendants ineligible for the 2(b) exemption. While the States do not believe that this ruling was sufficiently inclusive of the conduct of all the reinsurers, it was certainly correct as to the conduct of the London-based defendants. Indeed, the record before this Court identifies not a single London-based reinsurer defendant that is licensed to engage or is engaged in the business of insurance in any of the relevant States. *Cf.* Sts. Reg. App., JA 225-50, ¶ E.

Moreover, under the holding of *FTC v. Travelers Health Ass'n*, 362 U.S. 293, 298-302 (1960), even if the states had attempted to regulate the conduct of the London-based reinsurers, such attempts would not have constituted "state regulation" as that term is used in section 2(b). In *Travelers Health* this Court considered what Congress meant by the term "state regulation" in



section 2(b) and held that the term does not refer to state regulation of activities carried on beyond the borders of the regulating state. 362 U.S. at 298-302. Thus, conduct qualifies for section 2(b) immunity only when it occurs within the borders of the very state that is seeking to regulate it.

In these cases, the conduct of the London-based reinsurers occurred in some states, as well as abroad, but not sufficiently within the borders of any one state for a state's attempts at regulation to be considered "state regulation" for purposes of section 2(b). Under the plain meaning of section 2(b) of the McCarran Act, this conduct must remain subject to scrutiny under the antitrust laws. Any other conclusion would create a void, unintended by Congress, where private, anti-competitive conduct was neither regulated by the state nor subject to review under the federal antitrust laws.

### B. Under established principles of conspiracy law, all conspirators are liable for antitrust injury flowing from the unregulated acts of their co-conspirators.

Under established principles of conspiracy law, all conspirators are responsible for the actions taken in furtherance of the conspiracy. *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 253-54 (1940). All conspirators are liable under Section 1 of the Sherman Act when they adopt a " 'conscious commitment to a common scheme designed to achieve an unlawful objective.' " *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 764 (1984) (citation omitted). This is true even if one of the conspirators otherwise enjoys an immunity from antitrust prosecution. *United Mine Workers v. Pennington*, 381 U.S. 657, 670 (1965).

Thus, even though a union and its members have antitrust immunity when making wage agreements with multi-employer bargaining units, it is also the case that:

> a union forfeits its exemption from the antitrust laws when it is clearly shown that it has agreed with one set of employers to impose a certain wage scale on other bargaining units. One group of employers may not conspire to eliminate competitors from the

> industry and the union is liable with the employers if it becomes a party to the conspiracy.

*Id.* at 665-66. In this sense, the labor exemption operates as an exemption for some, but not all, conduct of labor unions just as the McCarran Act grants an exemption for those entities engaged in the business of insurance to the extent such business conduct is regulated by the states.

Defendants try to avoid the obvious analogy between labor exemption cases and their conduct by claiming that the labor exemptions, unlike the McCarran Act, apply to entities rather than conduct. Hartford Br. 23. This argument is in error. The labor exemptions explicitly immunize conduct of labor unions and their members, and not the entities themselves. *See, e.g., Pennington*, 381 U.S. at 661-62 (Section "20 of the Clayton Act, 38 Stat. 738, [29 U.S.C. § 52] and § 4 of the Norris-LaGuardia Act, 47 Stat. 70, [29 U.S.C. § 103] permit a union, *acting* alone, to engage in the *conduct* therein specified without violating the Sherman Act.") (emphasis added); *see also, e.g.*, 29 U.S.C. § 52 (limiting injunctive relief against a union engaging in numerous activities such as peaceably assembling, persuading others by peaceful means); 29 U.S.C. § 103 (limiting injunctive relief against "yellow dog" contracts); 29 U.S.C. § 104 (limiting injunctive relief against unilateral or concerted conduct, including refusals to work, to assemble or to join a union). Various insurance *amici curiae* apparently accept this mainstream interpretation of the labor exemption.[41]

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[41] According to the Brief Amici Curiae of the National Association of Casualty & Surety Agents, *et al.*, at 13 ("NACSA Br.") (emphasis original):

> The labor union cases cited in . . . *Royal Drug* hold only that agreements with non-exempt entities lose the traditional labor-union immunity *if* they are not the kind of agreements that the exemption was intended to protect. Thus, it is "beyond question that a union may conclude a wage agreement with a multi-employer bargaining unit without violating the antitrust laws," and the immunity is not available only for *certain types of agreements* with non-exempt employers.



Even where an otherwise exempt labor union engages in conduct where the "goal is legal" and within the purview of the exemption, the union cannot claim exemption when the *means* used constitutes a "direct restraint on the business market [and] has substantial anticompetitive effects, both actual and potential, that would not flow naturally from the elimination of competition over wages and working conditions." *Connell Construction Co. v. Plumbers & Steamfitters Local Union No. 100*, 421 U.S. 616, 625 (1975).

Defendants' formulation of the issue before this Court erroneously presupposes that once an entity engages in exempt conduct, it is shielded from liability for antitrust injuries caused by *any* conduct to which it agrees. This formulation, if adopted, would transform the McCarran Act exemption into something it is not – an entity exemption. *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 210 (1979) (section 2(b) of the McCarran Act exempts the business of insurance from antitrust scrutiny, not the business of insurers). Defendants' formulation must be rejected, therefore, because it ignores settled conspiracy law making each of them liable for the antitrust injuries that flow from their joint agreement to engage in unregulated acts. *See Socony Vacuum Oil Co.*, 310 U.S. at 253-54.

Thus, the States do not seek a ruling in any way new to established conspiracy law. To the contrary, the States merely seek a ruling that the McCarran Act exemption does not extend to agreements between insurers and reinsurers pursuant to which reinsurers undertake unregulated conduct causing antitrust injury. Given the lack of state regulation of the reinsurers' conduct and their co-conspirators' participation in it, this ruling would not expose legitimate, regulated, joint action between such companies to antitrust scrutiny.

### C. Defendants' expansive reading of section 2(b) of the McCarran Act threatens effective state regulation of the insurance industry.

Application of the federal antitrust laws to defendants' conduct would strengthen state regulatory schemes by foreclosing opportunities to evade them. State insurance regulators are aware of the potential for gaps between state

regulation and the application of federal law.[42] The plain language of the McCarran Act does not countenance such "gaps" and clearly applies federal law "to the extent" the states do not regulate the business of insurance. A contrary ruling would create a zone of conduct that is neither regulated by the states nor subject to the antitrust laws. Congress did not intend such a void.[43]

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[42] In recent Congressional hearings, state regulators have requested federal assistance in "filling the gaps in current state regulation." One such gap, it was noted, exists with respect to "alien reinsurers located outside the United States and not licensed anywhere in the United States . . . [s]ince a reinsurer does not have to be licensed in the state in which it does business . . . ". Specifically, representatives of the California, New York and Texas Departments of Insurance called for "federal registration/certification of offshore, alien insurance and reinsurance companies" together with "federal sanctions for violating those new requirements." Permanent Subcommittee on Investigations of the United States Senate Committee on Governmental Affairs, *Second Interim Report on the U.S. Government Efforts to Combat Fraud and Abuse in the Insurance Industry: Problems with the Regulation of the Insurance and Reinsurance Industry*, Senate Report 102-310, 102nd Cong., 2d Sess. (July 1, 1992), at 7, 8, 23-24.

[43] Some have argued that Congress fully intended section 2(b) to be interpreted consistently with this Court's decision in *Parker v. Brown*, 317 U.S. 341 (1943). *See, e.g.*, Weller, *The McCarran-Ferguson Act's Antitrust Exemption for Insurance: Language, History and Policy*, 1978 Duke L.J. 587, 615-19 *et seq.* Although this issue need not be reached in order to reject petitioners' argument that the states "regulated" reinsurer conduct, it is a position with considerable support in the legislative history of the McCarran Act. The repeated references during the Senate debates to the requirement that the states "affirmatively," "specifically" and "adequately" regulate before the federal antitrust laws are displaced are fully consistent with a codified *Parker* doctrine interpretation. *Id.* The principal proponent of the compromise bill which ultimately passed, the National Association of Insurance Commissioners, *id.* at 593-95, stated that the McCarran Act "is based in a general way, upon . . . *Parker*." *Id.* at 617, *citing*, NAIC Memorandum of Explanation, *reprinted in* 90 Cong. Rec. A4407 (1944). Indeed, it would seem anomalous for this Court to conclude as it did in *FTC v. Ticor Title Ins. Co.*, 112 S. Ct. 2169 (1992), that the state regulation of title insurer search and examination fees was insufficient for "active



Far from intruding on state interests in policing regulated activity, this straightforward reading of the McCarran Act underscores the "cooperative federalism" which underlies much state insurance regulation. *Cf. FTC v. Ticor Title Ins. Co.*, 112 S. Ct. 2169 (1992).[44] States have increasingly relied upon competition to supplement insurance regulation. The McCarran Act explicitly acknowledges the primacy of state regulation where states can and do regulate, even if a state's regulatory scheme has a profound, adverse effect on competition. Consistent with these same principles, the States ask no more than that this Court protect their right to rely on competition in insurance markets they choose not to regulate or cannot in fact regulate.[45]

Defendants ignore the plain language of the statute when they argue that because state regulators have authority to disapprove terms and conditions of primary insurance, they

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supervision" yet the lack of *any* state review *under the same statute* of reinsurance boycotts was sufficient for McCarran Act purposes.

[44] For example, the rating bureau statute under which the title insurers in *Ticor* were licensed is the same statute under which petitioner ISO is licensed. *See, e.g.*, ch. 625, Wis. Stats. Wisconsin, and states with similar statutes, "presume" that the markets in which insurers make business decisions are competitive. "On the whole, the insurance market is fairly competitive and attention directed to making it more so will be more rewarding than effort directed to the regulation of particular rates." Wis. Stat. Ann. § 625.01.

[45] Additionally, the Act counsels that federal antitrust law is displaced only when state regulation would be "invalidated, impaired or superseded". 15 U.S.C. § 1012(b). *See also United States v. Crocker Nat'l Corp.*, 656 F.2d 428, 452-55 (9th Cir. 1981), *rev'd on other grounds sub nom, BankAmericard Corp. v. United States*, 462 U.S. 122 (1983); Weller, *supra* n.43, 1978 Duke L. J. at 602-06. There is no conflict between state regulation and the application of the federal antitrust law to the defendants' conduct in these cases. *Cf. Silver v. New York Stock Exchange*, 373 U.S. 341 (1963).

must also be held to have regulated the agreements to withhold reinsurance which "affected" those terms and conditions. Hartford Br. 17. Defendants cite no authority for this proposition.

Under the plain language of the McCarran Act, the antitrust laws are "applicable to the business of insurance *to the extent* that such business is not regulated by state law" 15 U.S.C. § 1012(b) (emphasis added). Defendants' approach nullifies the emphasized language and creates a regulatory void. Defendants would deem all conspiracies – no matter how substantial the effect and no matter how far beyond the purview of state regulators – regulated for purposes of the McCarran Act if states regulate, even unknowingly, some consequence of the conspiracy.[46]

Finally, defendants and their amici argue that under the ruling of the court of appeals, insurance companies would lose their McCarran Act immunity whenever they consult or participate with any unregulated entity in forms development and other "vital" activity. *See* Hartford Br. 19-22; NACSA Br. 6-9. In making this argument, defendants change the focus from the actual conduct challenged here – unregulated reinsurers' coercive withholding of reinsurance – to *all dealings with reinsurers*.[47] The focus in determining whether the "state

[46] Defendants' assumption that States can disapprove any insurance form "they determine to be the product of anti-competitive practices" is also unwarranted. *See* Hartford Br. 17. States cannot adequately assess the conduct of reinsurers that are outside their jurisdiction. The requirement of state regulation for section 2(b) purposes cannot be satisfied unless a state has the means to assert direct control, within its own boundaries, over the party engaging in the challenged conduct. *See Travelers Health Ass'n v. FTC*, 298 F.2d 820, 823 (8th Cir. 1962) *on remand from* 362 U.S. 293, 297 (1960).

[47] When defendants do specify conduct, they mischaracterize the conduct as the domestic insurers' participation in "joint activity with foreign reinsurers to establish terms and conditions of insurance". Hartford Br. 15. Similarly, amici mischaracterize the challenged practice as "the manner in which an advisory organization formulates advisory policy forms." NACSA Br. 8.



regulation" requirement is met, however, belongs on the "particular activities at issue" rather than on some generalized category of conduct. *See* Brief for the United States as Amicus Curiae on Petition for a Writ of Certiorari at 9.

The Ninth Circuit ruling means only that the antitrust laws are applicable to agreements to engage in the *unregulated* business of insurance. An insurance company's discussions and agreements with "consumer groups, corporate risk managers, and policyholder representatives," Hartford Br. 21, are regulated. Hence, such dealings would retain their McCarran Act exemption under the Ninth Circuit's ruling. Contrary to defendants' argument, insurers need not abandon all "state-authorized" agreements. Insurers need only abandon unauthorized, unregulated agreements with reinsurers for reinsurers to engage in anticompetitive acts that cause antitrust injury to American consumers.

In any event, the unavailability of the McCarran Act exemption does not automatically impose antitrust liability on insurers for joint conduct with reinsurers. If an insurer has no exemption with respect to certain conduct, that conduct simply becomes subject to antitrust scrutiny, not necessarily antitrust liability.[48]

Most companies have no trouble discerning the difference between lawful agreements regarding the supply of important inputs and unlawful agreements to deny competitors such inputs unless the competitors accept particular terms of doing business. The court of appeals' decision leaves insurers free to purchase reinsurance but properly warns them against using such arrangements as exclusionary devices directed against competitors.

[48] Agreements between insurers and reinsurers are akin to purchase and sale agreements between vertically related firms in any other industry. Reinsurance is an input into insurance, the finished product. An insurer purchasing reinsurance is simply securing an input into the finished product. That type of transaction is ordinarily not an antitrust violation.

## III. BECAUSE THE INSURERS PARTICIPATED IN A NON-EXEMPT CONSPIRACY, THE ANTITRUST LAWS APPLY TO ALL CONDUCT IN FURTHERANCE OF THAT UNLAWFUL CONSPIRACY.

As discussed above, the insurers can be held liable as co-conspirators for any antitrust injury caused by the reinsurers' anticompetitive acts. A separate question is presented when additional antitrust injury flows independently from the insurers' regulated conduct in furtherance of the otherwise unlawful conspiracy. As to such additional antitrust injury, the McCarran Act exemption is inapplicable because that regulated conduct both furthered the conspiracy and relied upon unregulated conduct. Loss of the McCarran exemption for acts in furtherance of an otherwise non-exempt conspiracy is wholly consistent with this Court's general principles of antitrust liability. "[I]t is well settled that acts which are in themselves legal lose that character when they become constituent elements in an unlawful scheme." *Continental Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 707 (1962).

When nominally exempt conduct furthers a non-exempt conspiracy, this Court has consistently held that the exemption is inapplicable to the specific conduct in furtherance of the unlawful conspiracy.[49] *See, e.g., Connell Construction Co. v. Plumbers & Steamfitters Local Union No. 100*, 421 U.S. 616, 625 (1975); *United Mine Workers v. Pennington*, 381 U.S. 657, 662 (1965); *Allen Bradley Co. v. Local Union No. 3*, 325 U.S. 797, 807-08 (1945). *See also Case-Swayne Co.v. Sunkist Growers*, 389 U.S. 384, 394 (1967); *National Broiler Marketing Ass'n v. United States*, 436 U.S. 816, 827-29 (1978).

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[49] When an entity commingles exempt and non-exempt conduct, the term "forfeiture" accurately describes the *loss* of the exemption for the otherwise exempt conduct. On occasion this Court has used the term "forfeiture" also to describe the *inapplicability* of the exemption to nominally exempt conduct undertaken in furtherance of a non-exempt agreement. *See, e.g., United Mine Workers v. Pennington*, 381 U.S. 657, 665-66 (1965).



Even in those cases where, unlike here, the *only* conduct of a party would nominally qualify for exemption, the exemption is inapplicable if that conduct is taken in furtherance of a non-exempt agreement. *See, e.g., Allen Bradley*, 325 U.S. at 799-800, 807-08 (defendant union had entered into nominally exempt collective bargaining agreements obligating local contractors to purchase electrical equipment only from local manufacturers with closed shops). This Court has easily found the labor exemption inapplicable when nominally exempt collective bargaining agreements undercut the purpose of the exemption – to allow unions to exercise independent judgment with respect to their bargaining policy. *Pennington*, 381 U.S. at 667-68.

The logic of the labor cases applies even more strongly in the context of McCarran Act immunity. *See Royal Drug*, 440 U.S. at 231 (citing labor and agricultural cooperative exemption cases in discussing McCarran Act "business of insurance" exemption).[50] When ISO and its members act jointly within the context of the state-authorized forms development process, they act consistently with the purposes of the McCarran Act exemption and state laws governing forms development. In this process, each competitor is free to bring its unique, competitive perspective to the forms development process authorized by state law. When insurers and reinsurers enter into unregulated, anticompetitive agreements to impose cartel terms, they move beyond the ambit of state regulation, crossing the line drawn by the McCarran Act's exemption.[51]

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[50] Agricultural cooperatives, normally immune from antitrust liability under the Capper-Volstead Act, 7 U.S.C. § 291, forfeit that immunity when acting in concert with entities not entitled to such protection. *Royal Drug*, 440 U.S. at 231, citing *Case-Swayne Co. v. Sunkist Growers, Inc.*, 389 U.S. 384 (1967); *United States v. Borden Co.*, 308 U.S. 188 (1939). When nominally exempt parties conspire with entities outside the intended *class* of those protected, these parties, in limited sense, act outside the intended scope of *conduct* protected by the Capper-Volstead Act.

[51] In *Allen Bradley*, this Court flatly rejected the argument that exempt conduct taken in furtherance of a non-exempt conspiracy ought to be permitted because of any perceived difficulty in drawing lines between

In the present cases, the voluntary, cooperative forms-development process contemplated by state law, *see, e.g.*, Conn. Gen. Stat. § 38-201j(b)(6), JA 230, yielded forms which the primary defendants opposed. Defendants then reached agreement with the unregulated reinsurers to directly impose the cartel's decision on an unwilling market. In addition, the primary defendants and their London-based co-conspirators targeted participants in the ISO process who had decided, prior to the infusion of the unregulated conduct, not to dismantle the forms and support services so essential to providing insurance products to the domestic market.[52] *Cf. Allied Tube & Conduit Corp v. Indian Head, Inc.*, 486 U.S. 492, 503 (1988) (coercive commercial conduct within the context of a voluntary product standardization process not immune merely because it is intended to influence governmental action).

The very purpose of state regulation and, hence, McCarran immunity, was defeated by defendants' conduct. When an

permissible and prohibited activities. *Id.* at 811. The Court stated that it could draw a line "with assurance" that any nominally exempt conduct would not be exempt where such conduct furthered an unlawful conspiracy. *Id.* The Court can draw a line in the McCarran Act context with even greater assurance because the nominally exempt conduct was in furtherance of an unregulated and, hence, non-exempt agreement. In the labor law context, there is no "state regulation" line and, hence, the Court has found it necessary to review the collective bargaining agreement in question. *See, e.g., id.*

[52] It would be equally objectionable if the unregulated conduct constituted "boycott, coercion or intimidation" or a different antitrust violation. For example, the exemption would be inapplicable where reinsurers agreed to price discriminate in favor of ISO members who, in exchange, agreed to switch their votes on a crucial ISO issue. Standard treaty or facultative reinsurance agreements would not, of course, be affected at all by such a holding because they do not constitute antitrust violations and because they do not call for conduct by insurers in furtherance of an otherwise unlawful agreement. *See generally* 1 B. Webb, J. Launie, W. Rokes & N. Baglini, *Insurance Company Operations*, 321-66 (1984).



insurer enters into an unregulated agreement, its incentives are altered in a way that will not be apparent to the regulators who review, at most, the end product of the joint activity. Thus, unregulated agreements undercut the very premise of competition underlying state regulation of the insurance industry. St. Reg. App., JA 225-50[53]; *see also, Ticor*, 112 S. Ct. at 2178.[54]

When Congress granted the states permissive power to regulate the insurance industry, it did not at the same time empower members of that industry to engage in joint conduct to impose their anticompetitive interests on each other or on the market as a whole. Members of the insurance industry may not install a private system through which they write their own regulations, adhere to them, and force others to do the same. Whether defendants engage in acts of boycott, coercion or intimidation, or otherwise involve themselves in unregulated reinsurance conduct, they subvert the operation of state regulation and engage in behavior outside the McCarran Act. Failure to apply the antitrust laws to this conduct would undercut the States' preference for competition in the insurance industry, would contradict the plain language of the McCarran Act, and would undermine Congressional intent in enacting that law.

## CONCLUSION

For the foregoing reasons, the decision of the court of appeals should be affirmed.

[53] The States' Regulatory Appendix includes for each state a section titled "[state] statutes express an overall policy disfavoring collusion and favoring competition in the provision of insurance coverages." *See, e.g.*, JA 226, 229, 237 and 243.

[54] Review of a form is not regulation of the use of that form. *See* States' Reg. App., JA 225-50, ¶ E. *See supra* n.46.

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